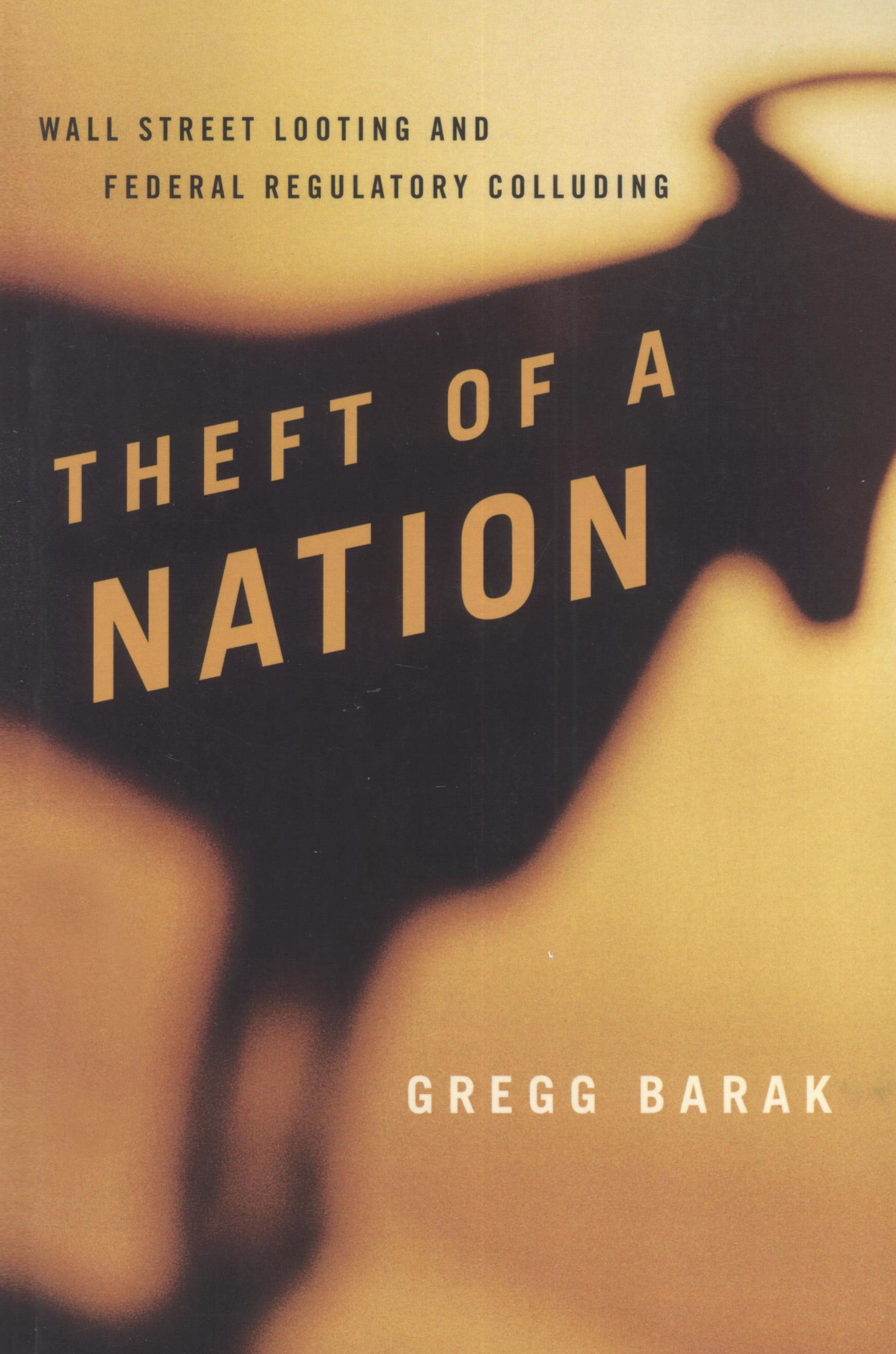
WALL STREET LOOTING AND
FEDERAL REGULATORY COLLUDING
THEFT OF A
NATION
GREGG BARAK

Theft of a Nation

Wall Street Looting and Federal Regulatory Colluding

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Praise for *Theft of a Nation*

"*Theft of a Nation* offers a rich history of regulation in the United States: the forces that promoted it; the forces that sought (and still seek) to undo it; the consequences of deregulation. Timely and insightful, *Theft of a Nation* will generate research for years to come."

—**GRAY CAVENDER**,
Arizona State University

"Finally! In *Theft of a Nation*, Gregg Barak reviews the actions that led to the so-called mortgage crisis on Wall Street in terms of their underlying criminality, not only of the individual economic players but also of the Wall Street system itself. This is a book that applies traditional (and Barak's new) criminological models so we can understand the underlying causes of systemic conduct that would, in any other context, be viewed as simple and blatant criminal conspiracies. I recommend it to all of us who are still trying to understand how our nation not only tolerated but also eventually rewarded the actors and the system—the thieves—that stole our nation's economic security."

—**HON. DONALD SHELTON**, chief judge,
Washtenaw Trial Court, Ann Arbor, Michigan

"This is an intelligent and disturbing analysis of how Wall Street interests and governmental policies have, time and again, colluded in the fleecing of America. It is nothing short of a tour de force in the areas of white-collar crime and victimology."

—**A. JAVIER TREVIÑO**, Wheaton College

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ISSUES IN CRIME AND JUSTICE

Series Editor
Gregg Barak, Eastern Michigan University

As we embark upon the twentieth-first century, the meanings of crime continue to evolve and our approaches to justice are in flux. The contributions to this series focus their attention on crime and justice as well as on crime control and prevention in the context of a dynamically changing legal order. Across the series, there are books that consider the full range of crime and criminality and that engage a diverse set of topics related to the formal and informal workings of the administration of criminal justice. In an age of globalization, crime and criminality are no longer confined, if they ever were, to the boundaries of single nation-states. As a consequence, while many books in the series will address crime and justice in the United States, the scope of these books will accommodate a global perspective and they will consider such eminently global issues such as slavery, terrorism, or punishment. Books in the series are written to be used as supplements in standard undergraduate and graduate courses in criminology and criminal justice and related courses in sociology. Some of the standard courses in these areas include: introduction to criminal justice, introduction to law enforcement, introduction to corrections, juvenile justice, crime and delinquency, criminal law, white collar, corporate, and organized crime.

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In memory of Glass-Steagall, 1933–1999

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Additionally, I would like to acknowledge "realist criminology," a research tradition that is both empirically based and theoretically driven, and "social constructionism," a sociological body of relative truth formation. Taken together the material realities of crime and justice are derived from those labels created by empirically grounded social interactions. These labels in turn have both symbolic meanings and practical consequences. First, they enable people to identify and distinguish between types of harms or social injuries. Second, when criminal events occur these labels facilitate the likelihood that "justice" is done or not.

For example, as philosopher of law Hyman Gross has argued in his classic work, *A Theory of Criminal Justice*, "The rules of conduct laid down in the criminal law are a powerful social force upon which society is dependent for its very existence."[1] Yet, from a social constructionist perspective, Wayne Morrison has emphasized in the British anthological textbook, *Criminology*, "It is a social choice to recognize such and such as a crime, or such and such a person as a 'criminal.' Some other term and therefore some other course of action could be used."[2] Or as the Dutch abolishment lawyer Louk Hulsman has pointed out, "Crime has no ontological reality. Crime is not the object but the product of

criminal policy. Criminalization is one of the many ways of constructing social reality."[3] At the same time, from the vantage point of realist criminology, crime is not only a social construction produced in tandem by control agents, mass media, and political ideologies. Crime is also a material phenomenon that has a reality of its own.[4]

Accordingly, the social problem of Wall Street securities fraud is as much a problem of how it is defined and represented as it is a matter of how finance criminal activities are organized and institutionalized across society. This inquiry that you are about to experience embodies an examination of both the realities and the representations of Wall Street looting and federal regulatory colluding.

Contents

Introduction

The U.S. Constitution mentions three federal crimes that citizens may be found guilty of: treason, piracy, and counterfeiting. At the turn of the twentieth century, this number had climbed to several dozen criminal statutes. By the 1980s the criminal code consisted of some three thousand offenses and twenty-three thousand pages of federal law. Today, nobody knows the exact number of offenses despite efforts at counting. According to a 2008 study there were an estimated forty-five hundred crimes in the federal code. In addition, there are thousands of federal regulations that carry criminal penalties. Many of the newly enacted federal laws have also lowered the bar for a conviction in that they no longer require the prosecutor to demonstrate the criminal intent of the defendant. For example, a 2010 joint study by the conservative Heritage Foundation and the liberal National Association of Criminal Defense Lawyers "analyzed scores of proposed and enacted new laws for non-violent crimes in the 109th Congress of 2005 and 2006. The study found of the 36 new crimes created, a quarter had no *mens rea* requirement and nearly 40% more had only a 'weak' one."[1]

As a result of these and other legal changes in punishment over the past thirty years, the U.S. Bureau of Justice Statistics reported that the total number of federal prisoners for 2009 had grown to two hundred thousand, representing more than an eightfold increase compared to a fourfold increase of state prisoners that grew to a little over two million.[2] The diminished requirements to prove criminal intent in order to convict, however, do not necessarily make the prosecutions of the crimes of the powerless or of the powerful any easier. For these legal developments are always subject to the vagaries of discretionary enforcement and selective application of the law.[3] At the same time, prosecutions are also subject to the number of street and suite crimes in

relation to the total systemic capacities of the agencies of crime control and financial regulation.

Rising criminal demand without increasing prosecutorial or penal capacity intensifies the inversely related criminal justice/punishment patterns of severity and leniency experienced by relatively powerless offenders versus the relatively powerful offenders. In effect, scarce resources result in criminal prosecutors selecting out those less demanding and more winnable legal cases. Demand and winnability are defined by the complexity of the involved illegalities and by the availability of potential defendants' resources.[4] Thus, the collective impact of system incapacity (i.e., scarce or shrinking resources) tends to suppress, or decrease, the likelihood of criminally prosecuting those complex white-collar offenses committed by persons with the deepest of financial pockets, like any of the Wall Street miscreants.

For example, as both the number of federal criminal statutes mushroomed in recent decades and the number of federal prosecutions rose annually from a little over 30,000 or 192 per one million adult citizens in 1980 to some 83,000 or 395 per one million in 2009, offenses prosecuted and offenders subject to criminalization and the penal sanction as indicated by the bar graph of the top ten federally prosecuted offenses for 2010 (see figure I.1) varied considerably. Some 63 percent of all those prosecuted and incarcerated were for immigration and drug-related offenses. Out of the total, only about 11.7 percent of these involved white-collar offenses, and the number of those convicted for fraud was 8,028.

None of those criminal prosecutions involved any of the wealthiest banks for securities frauds,[5] precluding one pathway to insolvency or bankruptcy. Moreover, in the wake of an epidemic of high-stakes financial fraud, Wall Street was brought to its knees only temporarily, thanks to the Troubled Asset Relief Program signed into law by President Bush on October 3, 2008. However, be-

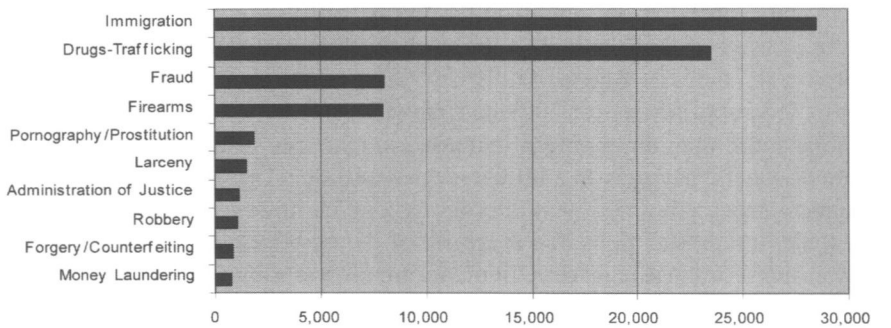

Figure I.1. Top 10 Federally Prosecuted Offenses in 2010. Adapted from "Tracking the Growth in Federal Criminal Sentences," U.S. Sentencing Commission, 2011.

fore and after the TARP bailouts, a larger pattern of collusion still exists in the forms of waivers and exemptions from punishment. These "plea bargain" deals have been negotiated between the mega investment banks of Wall Street, the Securities and Exchange Commission, and the U.S. Department of Justice in numerous agreements and settlements pertaining to securities fraud.

The relative incapacities of the systems of criminal and civil/regulatory bureaucracies that normally address the separate and related worlds of street crime and suite crime are also affected by the recent appellate and U.S. Supreme Court decisions regarding corporate liability and victim compensation involving security violations.[6] Other legal and political developments have specifically protected "crimes of capital accumulation" from aggressive prosecution, effectively establishing a non-criminal reality where banking and related investment frauds are, in effect, *beyond incrimination*.[7] Notwithstanding politics, law enforcers are not pursuing Wall Street fraud for several reasons:

- Statutes of limitations on securities litigation are effectively three years.
- Deferred prosecution agreements were established under the new 2008 guidelines of the U.S. Department of Justice that allow financial companies to avoid indictments if they agree to investigate and report their own crimes.
- The Securities and Exchange Commission and other federal/state regulators are not up to the potential case demand because of inadequate agency resources and staffing.
- The revolving door between the government-private sectors has created a situation in financial litigation where the ties between the DOJ and the white-collar-corporate legal defense community have become particularly strong.
- To pursue these securities frauds criminally would not only potentially bring about the demise of these financial institutions but in the process would also certainly hurt investors.

Bottom line: The federal prosecution of financial fraud in the United States by the end of 2011 had fallen to a twenty-year low. In fact, 2011 recorded the lowest number of securities fraud prosecutions in at least two decades. Trend wise, every year since 1999, the number of federal criminal prosecutions has gotten smaller and smaller as the banking oligopoly in the United States has gotten bigger and bigger. According to a recent Transactional Records Access Clearinghouse (TRAC) report from Syracuse University, the Department of Justice was on track to file just 1,365 prosecutions for financial institutional fraud in fiscal year 2011. At the same time, during 2011 the Securities and Exchange Commission filed a record-high 735 enforcement actions, going to trial in 19 cases, settling as many cases as possible with fraudulent defendants who neither admit nor deny wrongdoing while they agree to pay fines worth a fraction of the losses to their investors.[8]

Theft of a Nation is about finance capital and institutionalized crime. This book explains how the federal government, despite its rhetoric to the contrary, came to dismiss the crimes of Wall Street and to rebuff the victims of Main Street.[9] It examines the means by which a combination of governmental actions and omissions absolved Wall Street bankers, mortgage lenders, and associated swindlers from any accountability for their criminally fraudulent behavior. More broadly, *Theft of a Nation* is the story of the cultural and ideological histories of investment banking and Washington, DC, and how the interdependent cooperation by the nation's economic and political elites enabled Wall Street not to be held liable for the millions of people it victimized, for the billions of dollars it looted from investors, and for the trillions in capital that it destroyed worldwide. Finally, within the circumstances of both a mature democracy and a free-market society, this book provides an explication of the contradictions between the forces of institutionalized financial crime and the forces of institutionalized regulatory control.

FRAMING THE CASE

Theft of a Nation is not only about financial fraud and its control. More fundamentally, it's about the interactions of law, power, and wealth. As Marx and Weber would have understood, this investigation is about the interplay of the developing political economy[10] and the bureaucratically rational legal state.[11] Both thinkers despite their different emphases would have agreed that it's a study in the structural contradictions of *bourgeois legality*. Specifically, it's about the ways that finance capitalists who have great wealth, prestige, and access to politicos at the highest levels of government were afforded ample opportunities to make, break, and neutralize, if not capture, the laws of regulation. It is also about how these financiers were able to push back against or circumvent those unacceptable regulations that manage to get passed into law.

This happens for essentially two reasons. First, within the worlds of monopoly and financial capital, Wall Street investment bankers have become the dominant economic players. Second, within the current rise of global capitalism, finance capital is both the product and generator of forces that are transforming the contradictory governmental processes of regulation and deregulation. Furthermore, because of the dominance of finance capital and the concentration of wealth into a small number of Wall Street firms and institutions, a banking oligopoly[12] or a banking cartel[13] now exists in the United States (see figure I.2).

For a quick historical perspective: Back in 1947 the federal "government sued 17 leading Wall Street investment banks, charging them with effectively

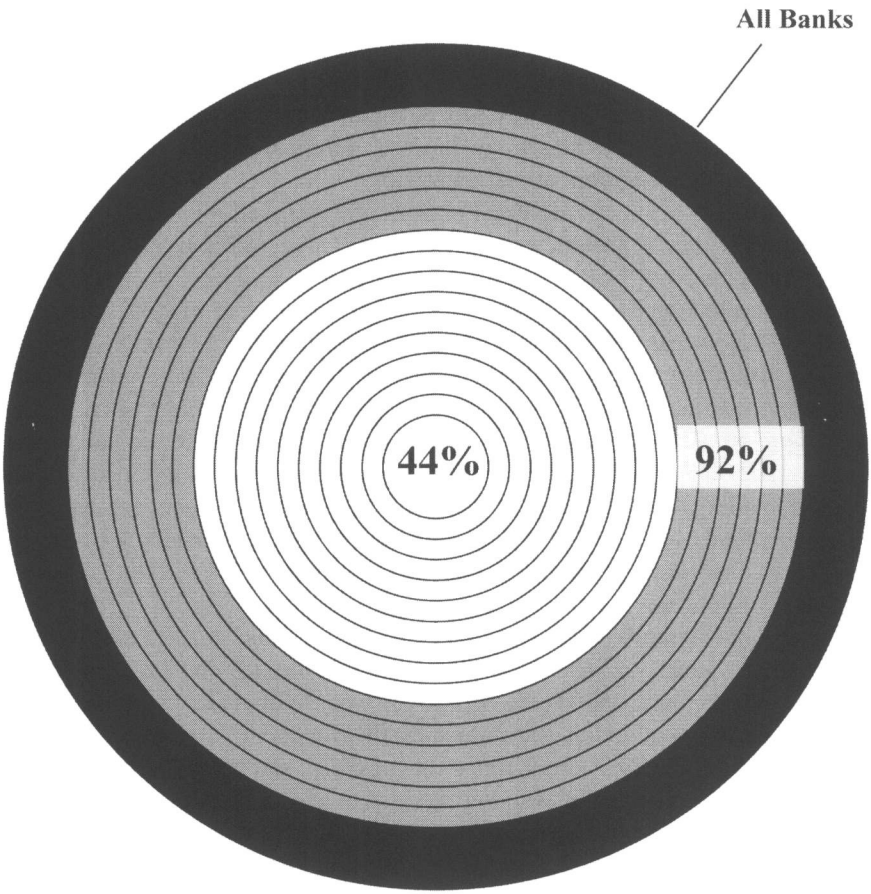

Figure I.2. The Banking Oligopoly in America. Represented in the banking oligopoly figure are the top three banks with 44 percent of market share, the top twenty banks with 92 percent of market share, and some eight thousand other banks dividing the remaining 8 percent of market share. From Barry Ritholtz, "The Big Picture," December 25, 2011, http://www.ritholtz.com/blog/2011/12/the-banking-oligopoly.

colluding in violation of antitrust laws."[14] The Department of Justice in its complaint alleged that these firms, among other things, had created "an integrated, overall conspiracy and combination" that began in 1915 and was in continuous operation thereafter, by which they developed a system "to eliminate competition and monopolize 'the cream of the business' of investment banking."[15] The United States argued further that these Wall Street investment banks, including Morgan Stanley as the lead defendant and Goldman Sachs, had created a cartel that set the prices charged for underwriting secu-

rities. The cartel also set the prices for providing mergers-and-acquisitions advice, while "boxing out weaker competitors from breaking into the top tier of the business and getting their fair share of the fees."[16] Finally, the government argued that the big firms had placed their partners on their clients' board of directors as a means of knowing what was coming down the pike internally and of keeping competitors at bay externally.

As journalist, former Wall Street banker, and best-selling author of *House of Cards*, *The Last Tycoons*, and *Money and Power*, William D. Cohan has recently contended, "The government was spot on" in their 1947 case: "The investment-banking business was then a cartel where the biggest and most powerful firms controlled the market and then set the prices for their services, leaving customers with few viable choices for much needed capital, advice or trading counterparties."[17] Today, the very same arguments can be made, only more so, as the capital worth of the leading firms (e.g., Goldman Sachs Group, Inc., Morgan Stanley, JP Morgan Chase & Co., Citigroup Inc., and Bank of America Corp.) is even more concentrated. In effect, this banking cartel or oligopoly with its political allies pretty much control what does or does not constitute securities violations in the world of fraudulently based market transactions.

More fundamentally, capitalism has always been a system of control and domination. Central to control and domination is the law and the state apparatus of enforcement that stands behind the law. Within the capitalist mode and relations of production, the state and law in tandem "operate to sanction the exploitation of direct producers—the workers—on behalf of the capitalists—the bourgeoisie—while giving the impression that state and law are in fact neutral, separate from the capital relation of exploitation."[18] This is not to imply that the interests of the state and of capitalists are one and the same. There are all types of competing interests within and between capitalists and state authorities. Thus, the state-legal criminalization of securities fraud hangs literally in the balance of the contradictory forces of free-market capitalism.

William Chambliss developed a *structural contradictions* theory of crime, law making, and enforcement.[19] This theory reflects the position that fundamental to all historical eras and societies are the contradictory forces of survival and destruction. While societies produce the means of survival, they also produce the means of decline, creating perpetual dilemmas and conflicts. Under free-market capitalism, the fundamental contradictions are between labor and capital. The laborers or employees pursue better working conditions and/or higher wages. Meanwhile, capitalists pursue greater profits and resist the demands of workers, as these will reduce their bottom lines.

Within the developing political economy of capitalism, the dilemma for capital, labor, and the state is how to reconcile their conflicts and differences,